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IN THE

Supreme Court of the United States

DAIMLERCHRYSLER CORPORATION,
Petitioner,

v.

CHARLOTTE CUNO, ET AL.,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

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BRIEF OF *AMICUS CURIAE* TAX FOUNDATION IN SUPPORT OF PETITION FOR A WRIT CERTIORARI

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BRIEF OF *AMICUS CURIAE* TAX FOUNDATION IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

INTEREST OF THE *AMICUS CURIAE*

The Tax Foundation submits this brief as *amicus curiae* in support of Petitioner in the above-captioned matter.[1]

The Tax Foundation is a non-profit research organization formed in 1937 to educate taxpayers about sound tax policy. In this regard, the Tax Foundation disseminates information on taxes and promotes tax systems that are simple, fair, and favor economic growth. The Tax Foundation works to further this mission by educating the legal community on economic issues relating to tax law, educating lawmakers and the public on tax law issues in an understandable and relevant manner, and promoting that judicial decisions on tax law advance economic growth and tax competition.

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[1] No counsel for a party authored this brief in whole or in part, and no person or entity, other than *amicus curiae*, has made a monetary contribution to the preparation or submission of this brief. Written consent of the Petitioner and Respondents have been obtained and filed with the Clerk of the Court.

SUMMARY OF ARGUMENT

This Court's guidance is needed to prevent immediate and permanent harm to commerce, particularly in Sixth Circuit states. The Court should grant certiorari because the Sixth Circuit's ruling imperils the ability of the states—especially those in the Sixth Circuit (Kentucky, Michigan, Ohio, and Tennessee)—to compete for investment. This case involves an important issue of federalism: It affects the balance of authority between the federal and state governments. The Sixth Circuit has severely limited states' autonomy in adopting their own competitive tax policies. Accordingly, this is exactly the kind of case this Court needs to decide.

This Court should also grant certiorari to provide needed clarity to its own decisions on the limitations imposed by the Commerce Clause on state tax authority. This Court's own sweeping language in several of its opinions serves, in part, as the basis for the lawsuit in this case. In fact, certain statements made by this Court, if taken literally, could serve as the basis for even more lawsuits in the future against other state tax and spending programs. This Court's review of this case is needed to clarify the standards for discrimination under the Commerce Clause.

Finally, this Court should grant certiorari to emphasize an important point: the Commerce Clause does not require a state to be more generous to out-of-state taxpayers than in-state taxpayers. The Sixth Circuit's focus on pre-existing tax liability and coercion would turn the Commerce Clause on its head and require Ohio to give investment tax credits only when an investor first comes to Ohio from another state, a ruling that cannot be squared with this Court's rulings that the Commerce Clause requires fair, not special, treatment of interstate commerce.

ARGUMENT

I. THIS COURT'S GUIDANCE IS NEEDED TO PREVENT IMMEDIATE AND PERMANENT HARM TO COMMERCE, ESPECIALLY IN SIXTH CIRCUIT STATES.

The Court should grant certiorari because the Sixth Circuit's ruling imperils the ability of the states—especially those in the Sixth Circuit (Kentucky, Michigan, Ohio, and Tennessee)—to

compete for investment. This case involves an important issue of federalism: It affects the balance of authority between the federal and state governments. The Sixth Circuit has severely limited states' autonomy in adopting their own competitive tax policies. Accordingly, this is exactly the kind of case this Court needs to decide.

The Sixth Circuit's decision invalidated a tax incentive properly enacted by Ohio. The decision represents a radical departure from any Commerce Clause case that has come before. This case has national implications that affect most corporations and most states in a major way. Indeed, nearly every state has an incentive on its books that is compromised by the Sixth Circuit's reasoning. *See* John C. Healy & Michael S. Schadewald, 1 2005 MULTISTATE CORPORATE TAX GUIDE: CORPORATE INCOME TAX 1-824 (2005) ("State competition for investment in new manufacturing plants and other business facilities is intense because of the economic growth it may foster. As a consequence, most states offer tax credits to companies that invest in facilities and create jobs in the state.").

Almost every major company benefits from those kinds of incentives. *See, e.g.*, Robert Guskind, *The New Civil War*, 25 NAT'L J. 817, 818 (1993) ("virtually every business contemplating a move or an expansion considers" incentives). And if the plaintiffs in this case properly had standing to sue, the Sixth Circuit's reasoning makes any taxpayer in the United States a potential plaintiff who could sue almost any major company in almost any state to challenge that company's receipt of an incentive.

This is not just speculation: As recently as last month, a lawsuit was filed in North Carolina challenging Dell Inc.'s right to $200+ million in tax credits. *Blinson v. North Carolina*, No. 05 CVS 8378 (Wake Co. Super. Ct., filed June 23, 2005). *See also Olson v. Kramer*, No. 62 C8 05 2727 (Ramsey County Dist. Ct., filed May 18, 2005) (citizen suit against tax incentives—the Job Opportunity Building Zones Program and Biotechnology and Health Sciences Zone Program—as violating the Commerce Clause by inducing business in tax favored zones in Minnesota rather than in another state); *DeCamp v. Nebraska*, No. 4:04 CV 03194 (D. Neb., filed May 18, 2004) (citizen suit claiming the tax incentive known as "Initiative 300" violates the Commerce Clause

by favoring farm families located in state over farm families located out of state).

Furthermore, the plaintiff's lawyers who brought the suit in Ohio have publicly stated that many other suits are in the works. *See* Amy Martinez, *Motion Challenges Dell Incentives*, NEWS & OBSERVER (Raleigh, N.C), June 24, 2005, at D1 ("Peter Enrich ... who filed the Ohio suit, said he's been approached by incentives opponents in five other states. He said all are seriously considering suing.")

State legislators and corporate decision makers need guidance in this matter. Uncertainty affects state legislatures' ability to legislate tax policy and it affects businesses' ability to rely on state tax laws to make investment decisions. Uncertainty itself is burdening the interstate commerce that the Commerce Clause is intended to protect. This Court should exercise its certiorari jurisdiction to restore certainty to state lawmakers.

A. Up Until the Sixth Circuit's Decision, the Commerce Clause Had Been Interpreted as Promoting Tax Competition.

The Commerce Clause of the United States Constitution gives Congress the plenary authority to "regulate Commerce ... among the several States." U.S. CONST. art. I, §8, cl. 3. The Commerce Clause, in the absence of congressional action, limits state actions that unduly burden interstate commerce. Indeed, this negative (or dormant) aspect of the Commerce Clause "prohibits economic protectionism—that is, regulatory measures designed to benefit in-state economic interests by burdening out-of-state competitors." *New Energy Co. v. Limbach*, 486 U.S. 269, 273–274 (1988). The lack of such a power under the Articles of Confederation, and the subsequent trade wars among the states, was the major reason the states gathered together to fix the Articles and, ultimately, replace them with the Constitution. *See* James Madison, *The Federalist No. 42*, *in* JAMES MADISON: WRITINGS 235, 238 (1999) ("A very material object of this power was the relief of the States which import and export through other States, from the improper contributions levied on them by the latter.").

Under its Dormant Commerce Clause jurisprudence, this Court has "...sustained a tax against Commerce Clause challenge when

the tax is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the State." *Complete Auto Transit v. Brady*, 430 U.S. 274, 279 (1977). Under the discrimination prong of *Complete Auto*, this Court has routinely struck down "tariff-like" tax schemes that levy discriminatory burdens on out-of-state businesses in an effort to benefit their in-state competitors. *See, e.g., West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186, 193 (1994) ("[t]he paradigmatic example of a law discriminating against interstate commerce is the protective tariff or customs duty, which taxes goods imported from other States, but does not tax similar products produced in State."); *H.P. Hood & Sons, Inc. v. Du Mond*, 336 U.S. 525, 539 (1949) ("[o]ur system, fostered by the Commerce Clause, is that every farmer and every craftsman shall be encouraged to produce by the certainty that he will have free access to every market in the Nation ....").

Indeed, a common thread running through this Court's decisions is that a state may not impose a taxing scheme that is a protectionist, tariff-like measure that favors in-state taxpayers or in-state interests by imposing tariff-like tax burdens on out-of-state taxpayers or out-of-state interests. For example:

- In *New Energy*, this Court invalidated an Ohio tax credit that favored ethanol produced in Ohio.
- In *Bacchus Imports*, this Court invalidated a Hawaii tax that favored an alcohol product produced in Hawaii. *Bacchus Imps., Ltd. v. Dias*, 468 U.S. 263 (1984).
- In *Boston Stock Exchange*, this Court invalidated a New York tax scheme on stock transfers in New York if the transferor used a New York stock exchange rather than an out-of-state stock exchange. *Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. 318 (1977).
- In *Westinghouse*, this Court invalidated a New York tax scheme that favored companies that exported a greater proportion of their products from points in New York than from points in other states. *Westinghouse Elec. Corp. v. Tully*, 466 U.S. 388 (1984).

In other words, the Dormant Commerce Clause prohibits tariff-like measures that interfere with the free flow of commerce and that interfere with tax competition.

The rationale for this prohibition is that competition "lies at the heart of a free trade policy...." *Boston Stock Exch.*, 429 U.S. at 336–337. The prohibition against tariff-like measures reflects the concern that if a tax burden "falls on economic interests without the state, it is not likely to be alleviated by political restraints which are normally exerted on legislation ... within the state." *McGoldrick v. Berwind-White Coal Mining Co.*, 309 U.S. 33, 45 n.2 (1940).

Still, this Court, in these decisions, has always emphasized that the Commerce Clause "does not prevent States from structuring their tax systems to encourage the growth and development of intrastate commerce and industry." *Boston Stock Exch.*, 429 U.S. at 336. To the contrary, this Court has emphasized that it is a "laudatory goal in the design of a tax system to promote investment that will provide jobs and prosperity to the citizens of the taxing State." *Trinova Corp. v. Michigan Dep't of Treasury*, 498 U.S. 358, 385 (1991).

In sum, the Commerce Clause encourages competition—including tax competition—among the states. As each state designs its own tax system to serve the needs of its citizens, each state will develop a tax system that is more or less attractive to different business investors. Businesses are then free to choose to locate in those states where the tax systems are most advantageous for production. *See* Charles M. Tiebout, *A Pure Theory of Local Expenditures*, 64 J. POL. ECON. 416, 418 (1956) ("The consumer-voter may be viewed as picking that community which best satisfies his preference pattern for public goods....The greater the number of communities and the greater the variance among them, the closer the consumer will come to fully realizing his preference decision.") (citations omitted). The only limitation on this is that a state cannot set up discriminatory tax regimes that act like protectionist barriers against interstate competition.

B. The Sixth Circuit's Ruling Uses the Commerce Clause as a Shield From Competition.

The Sixth Circuit's decision represents a significant departure from precedent. Indeed, there is no "tariff-like" tax implicated in this case. Instead, the Ohio taxpayers who brought this suit have turned the Commerce Clause on its head. They want to use the Commerce Clause to protect themselves from competition with interstate taxpayers.

The interests of the plaintiffs who brought the suit are important—those interests say a lot about the Commerce Clause claim itself. Usually, Commerce Clause challenges come from out-of-state business interests claiming unfair treatment that favors in-state business. In *Boston Stock Exchange*, stock sales in Boston were harmed by a New York law that protected the New York Stock Exchange. *Boston Stock Exch.*, 429 U.S. at 327–331. In *Bacchus Imports*, alcohol produced outside Hawaii was harmed by a Hawaii law that protected Hawaii-produced alcohol. *Bacchus*, 486 U.S. at 270–272. In *Westinghouse*, exports from points outside New York were harmed by a New York law that favored exports from points within New York. *Westinghouse Elec.*, 466 U.S. at 392–394. Indeed, it is not surprising that Commerce Clause challenges typically come from out-of-state businesses claiming unfair treatment that favors in-state interests—it is those out-of-state interests that are particularly vulnerable to discrimination because they do not have political power in the state. *See McGoldrick*, 309 U.S. at 45, n.2.

This case, therefore, is peculiar because of the unique identity of the parties who have brought the case: Ohio taxpayers have sued a multi-state business in an effort to protect themselves from tax competition in Ohio. No such case has come up before. *See* Peter D. Enrich, *Saving the States From Themselves: Commerce Clause Constraints on State Tax Incentives for Business*, 110 HARV. L. REV. 377, 381 (1996) ("the Court has not had occasion to address a challenge ... that a state tax provision's primary purpose or effect is to attract business to ... the state"). This is telling. As Justice Stevens has observed, where, as here, there has been an "absence of any previous challenge to such programs," such an absence is evidence of the fact that the "common and correct interpretation of the Commerce Clause as primarily intended to inhibit ...

restrictions on the free flow of goods within the national market rather than to provide the basis for questioning a State's right to experiment with different incentives...." *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794, 817 (1976) (Stevens, J., concurring).

In this first-of-a-kind challenge, it is clear that the Ohio taxpayers who brought this suit are not interested in the free flow of commerce. Indeed, their lawyers concede that is not what this case is about. Instead, they have explicitly stated that their intention is to "protect Ohio from Ohio." In fact, Mr. Enrich, one of the plaintiff's lawyers, tells us exactly why he brought this case:

> If all the states would refrain from deploying location incentives for businesses, then they all could retain more robust tax bases to support other governmental functions. But, if the other states are going to offer a widening array of tax breaks, then none could afford the costs -- more political than economic -- of abstaining. As a result, incentives proliferate, leaving all of the states worse off.

Enrich, *supra*, 110 HARV. L. REV. at 396; *but see* Clayton P. Gillette, *Business Incentives, Interstate Competition, and the Commerce Clause*, 82 MINN. L. REV. 447, 448 (1997) ("The very claim that competition for business location will have a negative impact seems odd. We typically think of competition as an effective mechanism for allocating scarce social resources to the party that values them most highly, and there initially seems little reason to believe that governmental bids vary from this principle.").

Of course the problem with this pointedly political argument is that it has no place in court. The plaintiffs have brought their case to court because they have found it difficult to advance their political agenda in the state legislatures. Enrich, *supra*, 110 HARV. L. REV. at 393–395 (explaining that it is politically difficult to get state legislatures to not compete for business investment with tax incentives). Yet the fact remains that this is a state-level political matter that must be decided by state legislators. Accordingly, the plaintiffs must fail. The Commerce Clause is not intended to second-guess a state's efforts to encourage investment. The Commerce Clause is not intended to protect Ohio from Ohio.

Unfortunately, the Sixth Circuit agreed with the taxpayers' novel position. The dramatic expansion of the Commerce Clause was unexpected and radical. The decision has had dramatic effects around the country. For one, companies are now uncertain as to whether they should rely on state incentives—validly passed by state legislatures—in making their decisions to invest in a state. For another, companies that have relied on these incentives are exposed to lawsuits from any taxpayer in any state who believes that the incentives violate the Commerce Clause, as interpreted by the Sixth Circuit. As discussed above, the companies' worries are well founded. Since the Sixth Circuit's decision, more lawsuits have been filed that challenge taxpayers' rights to the benefits of these incentives. And even more are coming.

C. Sixth Circuit States, in Particular, Need This Court's Guidance or They Will be Unable to Compete.

States vigorously compete for investment in today's economy. Despite cries of opposition to offshore "outsourcing", data from the U.S. Department of Labor indicates that most "outsourcing" involves a business moving a job from one state to another.

> Three out of four [layoff] events (90 out of 119) associated with movement of work occurred among establishments within the same company. In more than 7 out of 10 cases, the work activities were reassigned to places elsewhere in the U.S. In the 29 events in which work activities were reassigned to another company under contractual arrangements, half of the instances involved relocation of work outside the U.S. and half to companies within the U.S.

U.S. Dept. Labor, *Extended Mass Layoffs Associated with Domestic and Overseas Relocations, First Quarter 2004* (June 10, 2004), *available at* http://www.bls.gov/news.release/reloc.nr0.htm; *see also* Sharon P. Brown, *Mass Layoff Statistics Data in the United States and Domestic and Overseas Relocation*, U.S. DEPT. LABOR (Dec. 2004), *available at* http://www.bls.gov/mls/mls relocation.pdf.

In an age when international businesses have the freedom to invest nearly anywhere in the world, states are seeking to provide a

number of features to attract new investment. These features include competitive tax rates on income, tax credits for in-state investment, favorable apportionment formulas, public services such as roads and highways, and direct subsidies. All of these measures, though not equally preferable from a political or economic perspective, are intended to induce business investment that will "provide jobs and prosperity to the citizens of the taxing State." *Trinova Corp.*, 498 U.S. at 385.

Forty-six states have investment tax credits and incentives similar to the Ohio investment tax credit struck down by the Sixth Circuit. *See DaimlerChrysler Corp. v. Cuno*, Pet. for Cert., (Supreme Court Case No. 04-1704) at 8, n.5. To compete with its sister states, the states of the Sixth Circuit maintain numerous location-based business tax incentives. Michigan has at least twelve different location-based business tax incentives, ranging from investment tax credits to minority business credits.[2] Kentucky has at least thirteen location-based business tax incentives ranging from skills training to industrial development.[3] Tennessee allows taxpayers to take up to four credits against

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[2] *See, e.g.*, Mich. Comp. Laws § 208.35a (Investment Tax Credit); Mich. Comp. Laws § 208.38g (Michigan Economic Growth Authority Credit); Mich. Comp. Laws § 208.37b (High Technology Credit); Mich. Comp. Laws § 208.38e (Apprenticeship Tax Credit); Mich. Comp. Laws § 208.37a (Enterprise Zone Credit); Mich. Comp. Laws § 208.37c (Qualified Jobs Credit); Mich. Comp. Laws § 208.38d (Brownfield Development Credit); Mich. Comp. Laws § 324.36109 (Credit for Property Taxes on Farmland Subject to Developer Rights Agreements); Mich. Comp. Laws § 208.38 (Credit for Contributions to Certain Charitable Institutions); Mich. Comp. Laws § 208.38c (Credit for Contributions to Community Foundations); Mich. Comp. Laws § 208.38b (Disability Compensation Credit); Mich. Comp. Laws § 208.39c (Historic Rehabilitation Credit).

[3] *See, e.g.*, Ky. Rev. Stat. Ann. § 141.405 (Skills Training Investment Tax Credit); Ky. Rev. Stat. Ann. § 154.22-050 (Rural Economic Development Credit); Ky. Rev. Stat. Ann. § 154.45-090 (Enterprise Zone Jobs Credit); Ky. Rev. Stat. Ann. § 154.26-090 (Economic Revitalization Credit); Ky. Rev. Stat. Ann. § 154.24-110 (Jobs Development Credit); Ky. Rev. Stat. Ann. § 141.065 (Unemployment Tax Credit); Ky. Rev. Stat. Ann. § 141.041 (Coal Manufacturing and Heating Credit); Ky. Rev. Stat. Ann. § 141.412 (Qualified Farming Operation Credit); Ky. Rev. Stat. Ann. § 154.20-258 (Investment Fund Tax Credit); Ky. Rev. Stat. Ann. § 154.34-080 (Reinvestment Tax Credit); Ky. Rev. Stat. Ann. § 141.390 (Recycling Equipment Credit); Ky. Rev. Stat. Ann. § 141.395 (Research Facilities Construction Credit); Ky. Rev. Stat. Ann. § 141.128 (Clean Coal Facility Credit).

business tax liability ranging from the building of day care facilities to the creation of jobs.[4] Ohio has, at minimum, fourteen location-based business tax credits, including the investment tax credit at issue in this case.[5]

Like incentives in all the other states, incentives offered by Ohio and the rest of the states in the Sixth Circuit share one feature in common: they require in-state activities by the taxpayer in order to benefit from the credit. For example, the Michigan single business tax credit for charitable contributions requires that the taxpayer give money to Michigan charities in order to qualify for the credit. *See* Mich. Comp. Laws § 208.38. Kentucky's unemployment tax credit allows a $100 credit for each unemployed person hired by the taxpayer, so long as the person is officially classified as unemployed by the state Department for Community Based Services. *See* Ky. Rev. Stat. Ann. § 141.062.

Political controversy does not surround all of the incentives offered by Sixth Circuit states, yet the Sixth Circuit's broad ruling would imperil them all. For example, Tennessee gives a tax credit for construction of a day care facility for employees, but only if the facility is licensed by the Tennessee Department of Human Services. *See* Tenn. Rev. Code § 67-4-2009(3)(A). This would naturally exclude Tennessee taxpayers who pay for day care facilities licensed by other states, in the same way that Ohio's investment tax credit withholds a benefit from Ohio taxpayers who

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[4] *See, e.g.*, Tenn. Code Ann. § 67-4-2009(4) (Industrial Machinery Credit); Tenn. Code Ann. § 67-4-2009(3) (Day Care Center Construction Credit); Tenn. Code Ann. § 67-4-2009(6) (Medical Supplies and Equipment Tax Credit); Tenn. Code Ann. § 67-4-2109(c)(2)(A) (Jobs Tax Credit).

[5] *See, e.g.*, Ohio Rev. Code Ann. § 5733.33 (Machinery and Equipment Investment Credit); Ohio Rev. Code Ann. § 122.15 (Edison Research and Development Credit); Ohio Rev. Code Ann. § 122.171 (Job Retention Credit); Ohio Rev. Code Ann. § 5733.42 (Employee Training Credit); Ohio Rev. Code Ann. § 122.658 (Brownfield Revitalization Fund Credit); Ohio Rev. Code Ann. § 5733.063 (Savings and Loan Credit); Ohio Rev. Code Ann. § 5733.064 (Recycling and Litter Prevention Donation Credit); Ohio Rev. Code Ann. § 5733.32 (Grape Producing Property Credit); Ohio Rev. Code Ann. § 5733.36 (Day Care Provision Credit); Ohio Rev. Code Ann. § 5733.37 (Day Care Center Credit); Ohio Rev. Code Ann. § 5733.38 (Day Care Reimbursement Credit); Ohio Rev. Code Ann. § 5733.43 (Maintenance of Active Grade Crossing Credit); Ohio Rev. Code Ann. § 5733.46 (Ethanol Plant Investment Credit); Ohio Rev. Code Ann. § 5733.49 (Venture Capital Fund Credit).

invest in machinery or equipment in other states. The Sixth Circuit's ruling would imperil the Tennessee day care tax credit and any other tax credit that seeks to encourage in-state investment (be it an auto plant or a day care center) by denying the credit for out-of-state investment. *See Cuno v. DaimlerChrysler, Inc.*, 386 F.3d 738, 743 (6th Cir. 2004) ("the business that chooses to expand its local presence will enjoy a reduced tax burden, based directly on its new in-state investment, while a competitor that invests out-of-state will face a comparatively higher tax burden because it will be ineligible for any credit against its Ohio tax.").

Meanwhile, outside the Sixth Circuit, such credits are not similarly compromised. This puts the states of the Sixth Circuit at a competitive disadvantage.

This Court should grant certiorari now to announce a single rule for all states. If nothing else, the Commerce Clause requires that all states compete under the same rules and restrictions.

II. THIS COURT SHOULD GRANT CERTIORARI NOW TO CLARIFY ITS OWN STANDARDS FOR DISCRIMINATION UNDER THE COMMERCE CLAUSE.

This Court's own language in several of its opinions serves, in part, as the basis for the lawsuit in this case. In fact, certain statements made by this Court, if taken literally, could serve as the basis for even more lawsuits in the future. This Court's review of this case is needed to clarify the standards for discrimination under the Commerce Clause.

For example, this Court has said that state tax policy must be such that business decisions are made "solely on the basis of nontax criteria." *Boston Stock Exch.*, 429 U.S. at 331. This Court has also stated that a state cannot adopt a tax policy that "foreclose[s] tax-neutral decisions." *Id.* These statements, if taken literally, mean that a state cannot develop a tax policy that encourages growth and investment. Not even tax rate reductions or exemptions would be allowed under this literal language. *See* Walter Hellerstein & Dan T. Coenen, *Commerce Clause Restraints on State Business Development Incentives*, 81 CORNELL L. REV. 789, 802 (1995) ("literalistic focus on key passages in the Court's opinions might suggest that 'all state inducement programs are likely to be unconstitutional'").

But on the other hand, this Court has made equally sweeping, and seemingly contradictory, statements in its decisions. For example, this Court has written that its decisions should not be read to "prevent the States from structuring their tax systems to encourage the growth and development of intrastate commerce and industry." *Boston Stock Exch.*, 429 U.S. at 336. This Court has written that a state may "enact laws pursuant to its police power that have the purpose and effect of encouraging domestic industry." *Bacchus*, 468 U.S. at 271. And this Court has written that a state "may try to attract business by creating an environment conducive to economic activity." *West Lynn Creamery*, 512 U.S. at 199 n. 15. These statements seem to endorse state tax measures that are designed to make a state more attractive to business. Yet these are exactly the types of provisions that the plaintiffs in this case are seeking to invalidate. *See* Enrich, *supra*, 110 HARV. L. REV at 387 (encouraging plaintiffs to sue to invalidate measures that "enhance a state's attractiveness as a place for business to locate their facilities and their jobs").

This Court should grant certiorari now. State legislators and corporate taxpayers in most states are eagerly awaiting this Court's guidance on a question of national importance that is at the very root of our federalist system of government: How much freedom do the states have to adopt their own tax policies? And once adopted, can taxpayers rely on the state tax laws?

A. This Court Should Grant Certiorari Now to Clarify That Most Discrimination Challenges Under the Commerce Clause Must be Evaluated on a Fact-Sensitive, Case by Case Basis.

In *Boston Stock Exchange*, this Court explained that its Commerce Clause jurisprudence "turns on the unique characteristics of the statute at issue and the particular circumstances in each case." *Boston Stock Exch.*, 429 U.S. at 329. Yet the Sixth Circuit, in striking down Ohio's investment tax credit, formulated an overly broad rule that cannot be limited to tax incentives. In ruling that Ohio's investment tax credit violated the Commerce Clause because it encouraged "further investment in-state at the expense of development in other states," the Sixth Circuit's rule would sweep in a host of tax reform measures and other development incentives. *Cuno*, 386 F.3d at 745. Indeed, all

state tax laws arguably have the potential to distort the decision-making process in some way. The Sixth Circuit's broad ruling is wholly inconsistent with this Court's admonition to adjudge discriminatory tax schemes on a narrow, ad hoc basis.

B. This Court Should Grant Certiorari Now to Clarify That a State Does Not Violate the Commerce Clause Simply by Making its Tax Climate Attractive to Business.

This case presents a valuable opportunity to clarify the uncertainty generated by this Court's past decisions. The Sixth Circuit's ruling rests upon language, taken out of context, from prior Commerce Clause decisions written by this Court. The absence of clear guidance has allowed the plaintiffs to seize upon certain language to convince the Sixth Circuit to strike down a state tax policy with which plaintiffs disagree.

Consider this Court's admonition that state tax laws be written so that business decisions are based "solely on the basis of nontax criteria." *Boston Stock Exch.*, 429 U.S. at 331. This language cannot be taken literally. For example, states routinely reduce generally applicable tax rates and occasionally eliminate taxes. These routine actions would run afoul of this Court's "solely on the basis of nontax criteria" language. Indeed, if Ohio had enacted a general tax rate reduction and the resulting rate were lower than other competing states, a business may well decide to locate in Ohio "on the basis of" tax criteria. Literally speaking, the rate reduction would violate this Court's own standard.

Likewise, such routine state actions may run afoul of a literal reading of the Sixth Circuit's decision. If Ohio had reduced its generally applicable corporate income tax rate, and if petitioner had invested in another state, the income from the investment would have been apportioned to that other state. *See, e.g.*, Ohio Rev. Code § 5733.01 (levying corporate franchise tax for the "privilege of doing business" in state and "owning or using a part or all of its capital or property in this state"); *Wilkins v. Cuno*, Pet. for Cert., (Supreme Court Case No. 04-1724) at 9 ("If an interstate business elects to locate new manufacturing machinery and equipment *outside* Ohio, its Ohio percentage will decrease."). Thus, under a regime of lower tax rates, instead of investment tax

credits, DaimlerChrysler would still have only been able to "reduce its existing tax liability by locating significant new machinery and equipment within the state" because it would not receive a similar reduction "in tax liability if it [located] a comparable plant and equipment elsewhere." *Cuno*, 386 F.3d at 743. Again, that cannot be the standard, yet that is what the opinion says.

Because of the potentially sweeping effect of these standards, many other state tax policy decisions are imperiled, especially in the Sixth Circuit. For example, Kentucky enacted a comprehensive tax reform plan this year, designed to spur in-state investment and provide a more business-friendly climate. *See* H.B. 272, 2005 Leg., Reg. Sess. (Ky. 2005). Ohio enacted a similar plan, swapping its corporate franchise tax for a gross receipts tax in an effort to further enhance in-state investment. *See* H.B. 66, 126th Gen. Assem., Reg. Sess. (Oh. 2005). Michigan is currently embroiled in debate over its Single Business Tax, with both sides advocating reductions or elimination to spur the state's lagging employment market. *See, e.g.*, Michigan Dept. Treasury, *Governor Granholm's Single Business Tax Plan Introduced*, (Mar. 8, 2005), *available at* http://www.michigantaxfairness.com/media clips/GovernorGranholmIntroduced.pdf ("Governor Jennifer M. Granholm...called passage of her Single Business Tax reform package critical to retaining and creating more jobs in Michigan."). Under the Sixth Circuit's ruling in *Cuno*, and even under this Court's own language in certain decisions, these measures are now suspect because they may succeed in their objective of encouraging in-state investment.

Furthermore, such a sweeping interpretation of the Commerce Clause is in tension with this Court's past support for similar types of state tax incentives. In *Moorman Mfg. Co. v. Bair*, 437 U.S. 267 (1978), this Court upheld against a Commerce Clause challenge a state's right to attract investment using single sales apportionment (SSA). SSA gives businesses a powerful incentive to locate new investment in the SSA state, since property and payroll no longer matter for income apportionment purposes. Thus, a business can invest in unlimited property and payroll and still apportion income based solely on in-state sales. Fourteen states have, or are steadily moving towards, single-sales apportionment for all or some taxpayers (compared to one state—Iowa—when the Supreme

Court decided the *Moorman* case).[6] Six states weight sales at least fifty percent or higher in their apportionment formulas.[7] This year, bills were introduced in five more states (including Michigan)[8] and enacted in four states[9] to move to full or modified single sales apportionment.

The *Moorman* case was decided on the fair apportionment prong of *Complete Auto*, however the dissent would have invalidated SSA on discrimination grounds. *See Moorman*, 437 U.S. at 289 ("application of Iowa's single-factor sales-apportionment formula, in the context of general use of three-factor formulae, inevitably handicaps out-of-state businesses competing for sales in Iowa.") (Powell, J., dissenting). If Ohio's investment tax credit, as the Sixth Circuit ruled, discriminates

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[6] *See, e.g.*, Conn. Gen. Stat. § 12-218(k)-(l) (provides single sales apportionment for manufacturers and broadcasters); H.B. 191, 148th Gen. Assem., Reg. Sess. (Ga. 2005) (phasing into a single sales factor apportionment in 2008); 810 Ill. Comp. Stat. 5/304(h); Iowa Code § 422.33(2)(b)(3) (provides single sales apportionment for the manufacture and sales of tangible personal property); H.B. 679, 2005 Reg. Sess. (La. 2005) (weighting sales at 100% as of 1/1/2006); Md. Code Ann. Tax-Gen. § 10-402(c)(2) (single sales factor for manufacturers); Mass. Ann. Laws ch. 63, § 38(k)(5) (single sales factor for manufacturers, defense contractors and mutual funds); Mo. Rev. Stat. § 143.451.2(2)(b) (companies may choose an evenly weighed or single formula); Neb. Rev. Stat. § 77-2734.05(1); N.Y. Tax Law § 210 (phasing into a single factor sales apportionment by 2008); Or. Rev. Stat. § 314-650 (phasing in a single sales apportionment by July 2008); S.C. Code Ann. § 12-6-2240 (a single factor gross receipts formula applied to service related industries); Tex. Tax Code Ann. § 141.001; Wis. Stat. § 71.04 – 71.45 (phasing in a single sales factor by 2008).

[7] *See, e.g.*, Ariz. Rev. Stat. Ann. § 43-1139 (phasing in a 60% sales factor in 2007, 70% in 2008 and 80% in 2009, as amended by H.B. 2139); Mich. Comp. Laws § 208.45a (weighting sales at 90%); Minn. Stat. § 290.191 (weighting sales at 75%); Ohio Rev. Code § 5733.05(B)(2) (weighting sales at 60%); Or. Rev. Stat. § 314.650 (weighting sales at 80%); Pa. Stat. Ann. tit. 72, § 7401(9) (weighting sales at 60%)

[8] *See, e.g.*, H.B. 2139, 47th Leg., 1st Reg. Sess. (Ariz. 2005) (proposed 100% sales apportionment by 2010, amended to apportion at 80% by 2009); H.B. 679, 2005 Reg. Sess. (La. 2005); H.B. 4973, 93rd Leg., 1st Reg. Sess. (Mich.) (proposing a single sales factor apportionment); S.B. 753, 84th Reg. Sess. (Minn.); H.B. 660, 84th Reg. Sess. (Minn.) (both bills proposing a 3% increase in sales factor apportionment until 100% is reached in 2014); H.B. 515, 189th Gen. Assem., Reg. Sess. (Pa.) (passed the House on May 10, 2005, applying a single sales factor apportionment to sales made in the state.)

[9] Arizona, Georgia, Louisiana and New York enacted their single factor or modified apportionment laws in 2005. See *supra*, notes 6 - 8.

against interstate commerce by discouraging out-of-state investment, SSA would also likely be guilty of the same discrimination. Indeed, the plaintiffs' lawyer sees it just this way. Enrich, *supra*, 110 HARV. L. REV. at 462 ("income tax apportionment methods that give special weight to the sales factor demand close scrutiny, notwithstanding the Court's 1978 decision.").

Indeed, single sales apportionment's impact on business investment will be qualitatively indistinguishable from Ohio's investment tax credit: they both work to reduce taxable income with respect to in-state investments in physical capital. Thus, the Sixth Circuit's broad ruling creates a tension with this Court's ruling in *Moorman* and leaves SSA susceptible to Commerce Clause challenge in the Sixth Circuit and in other states that follow its reasoning. *See* Sylvia Dennen & Christopher Whitney, *Single Factor—Multiple Questions*, 2005 STATE TAX NOTES TODAY 19-2, Jan. 12, 2005 ("[i]t would appear that [Pennsylvania's single sales factor legislation] has quite a bit in common with the investment tax credits found to be unconstitutionally discriminatory ... in *Cuno*").

This Court's guidance is needed to clarify that these kinds of state tax policy decisions are, in fact, not objectionable.

III. THIS COURT SHOULD GRANT CERTIORARI NOW TO CLARIFY AN IMPORTANT POINT: THE COMMERCE CLAUSE DOES NOT REQUIRE A STATE TO BE MORE GENEROUS TO INVESTMENTS FROM "NEW" TAXPAYERS THAN INVESTMENTS FROM "OLD" TAXPAYERS.

The Sixth Circuit upheld Ohio's personal property tax exemption even while striking down Ohio's investment tax credit. The Sixth Circuit distinguished the exemption from the credit, holding that "[u]nlike an investment tax credit that reduces pre-existing income tax liability, the personal property exemption does not reduce any existing property tax liability." *Cuno*, 386 F.3d at 747. Thus, according to the Sixth Circuit, Ohio's personal property tax credit did not discriminate "against interstate commerce by coercing businesses already subject to ... Ohio ... tax to expand locally instead of out-of-state." *Id.* at 743.

This "pre-existing liability" formulation is regrettable. If taken literally, it suggests that a taxpayer who had no connection (or "nexus") with Ohio and moved into Ohio and who, in connection with its move into Ohio qualified for the investment tax credit, could keep the investment tax credit because the investment tax credit would not reduce any "pre-existing liability." Yet a taxpayer who already had nexus with Ohio and who qualified for the investment tax credit could not keep it because it would unconstitutionally reduce a "pre-existing liability."

Certainly this cannot be right. This Court has consistently interpreted the Commerce Clause to require fair and equal treatment of intrastate and interstate commerce: "A cardinal rule of Commerce Clause jurisprudence is that [no] State...may impose a tax which discriminates against interstate commerce...by providing a direct commercial advantage to local business." *Bacchus*, 486 U.S. at 268 (internal quotations omitted). Though the Commerce Clause forbids discriminatory treatment of out-of-state taxpayers, this Court has never interpreted it to require that states treat investment flowing into or out of a state more favorably than purely in-state investment.

> [T]he Commerce Clause surely does not impose on the States any obligation to subsidize out-of-state business ... [w]hether the encouragement takes the form of a cash subsidy, a tax credit, or a special privilege intended to attract investment capital, it should not be characterized as a "burden" on interstate commerce.

Hughes, 426 U.S. at 815–816 (Stevens, J., concurring).

The Sixth Circuit's decision would reverse course and require states to give more favorable tax treatment to investment flowing from out-of-state sources, without pre-existing tax liability, than investment flowing from in-state sources with preexisting liability. *See* Edward A. Zelinsky, *Cuno v. DaimlerChrysler: A Critique*, 2004 STATE TAX NOTES TODAY 192-2 (Oct. 4, 2004) ("Why should the Commerce Clause deny DaimlerChrysler an Ohio investment tax credit because of its old Ohio plant while the clause permits a credit for new investment to an otherwise identical competitor without an extant facility in Ohio?"). If Ohio's investment tax credit discriminates because it is more likely to induce Ohio businesses with "pre-existing" liability to invest in

Ohio as opposed to another state, then surely there is no constitutional infirmity if a business with no pre-existing tax liability invests in Ohio and takes the credit. The Sixth Circuit's ruling would require a state to discriminate *against* investment from resident sources in favor of out-of-state investment, a result that cannot be squared with this Court's insistence that the Commerce Clause requires neutrality between intrastate and interstate commerce.

This "pre-existing" formulation is particularly unhelpful with regard to transaction taxes, like the one at issue in *Boston Stock Exchange*. *Boston Stock Exch.*, 429 U.S. at 319. In that case, a reduced tax rate on securities transferred in New York was contingent on the taxpayer making the security sale there. That incentive was held unconstitutional But under the Sixth Circuit's "pre-existing liability" formulation, would New York's incentive still be unconstitutional—insofar as it encouraged taxpayers that did not transfer *or* sell securities in New York (i.e., had no "pre-existing" liability) to move both of those operations into New York and thereafter both transfer and sell securities there? Certainly this is not within this Court's reasoning in *Boston Stock Exchange*.

Yet, despite the fact that it is not a workable legal standard, the "pre-existing" formula will be the law in the Sixth Circuit unless this Court reviews this case. Further still, other jurisdictions may adopt this unworkable standard: The "pre-existing liability" shorthand has been used by commentators as a way of analyzing tax schemes for discrimination. *See, e.g.*, Heilerstein & Coenen, *supra*, 81 CORNELL L. REV. at 807 ("those ... incentives framed not as exemptions from ... *existing* state tax liability [are acceptable]"). It is likely, therefore, that without this Court's guidance, many legislators will try to incorporate the unworkable "pre-existing liability" standard into their tax schemes and many state courts will use this standard to analyze the constitutionality of state taxes.

Accordingly, this Court's guidance is needed now to avoid the effects of such an unworkable standard.

CONCLUSION

For the foregoing reasons, the Court should grant the petition for a writ of *certiorari*.

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